



Audit Report



OIG 05-033

**FinCEN: Heightened Management Attention Needed Over
Longstanding SAR Data Quality Problems**

March 23, 2005

**Office of
Inspector General**

Department of the Treasury

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Abbreviations

DI	Depository Institution
FinCEN	Financial Crimes Enforcement Network
IRS	Internal Revenue Service
LEA	Law Enforcement Agency
MSB	Money Service Business

Contents

OIG	Office of Inspector General
SAR	Suspicious Activity Report

*The Department of the Treasury
Office of Inspector General*

March 23, 2005

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The Financial Crimes Enforcement Network (FinCEN) has specified responsibility for administering the Bank Secrecy Act (BSA). A vital aspect of FinCEN's responsibility is the collection and maintenance of suspicious activity reports (SARs) filed by financial institutions. Law enforcement agencies use SARs to identify potential investigative leads to financial crimes such as money laundering and terrorist financing. Aggregated SAR data is also analyzed to identify trends and emerging criminal activities, as well as developing intelligence data. Nearly 1.5 million SARs have been filed with FinCEN from April 1996 through December 2003.

Our audit objective was to assess the status of FinCEN's implementation of their management corrective action plan in response to our December 2002 report entitled *FinCEN: Reliability of Suspicious Activity Reports*, OIG-03-035. In that report, we raised concerns over longstanding SAR data quality problems. We reported that these data problems could adversely affect FinCEN's ability to meet their core mission relative to the BSA and attendant money laundering programs.

We conducted our audit fieldwork at FinCEN headquarters in the Washington, D.C., area, and also at the Internal Revenue Service's (IRS) Detroit Computing Center (DCC) in Detroit, Michigan where SARs are collected and maintained on an automated data system. We also statistically sampled and reviewed over 400 SARs filed over a 12 month period ending October 2003. In reviewing the SARs, we focused on those data fields that law enforcement agencies (i.e., SAR users) advised us as being critical pieces of information for developing criminal investigative cases and or trend analysis. We also contacted 15 financial institutions from the sampled SARs to discuss our SAR observations. Finally, we met with several members of Treasury's BSA Advisory Group regarding

SAR data reliability problems¹. A detailed description of our audit objectives, scope and methodology is provided in Appendix I.

Results in Brief

In December 2002, we reported that the SAR data base contained incomplete and inaccurate data, as well as over 3,000 duplicative SAR filings². We attributed these data quality problems to several causes including data entry errors for paper filed SARs, filer errors, and inadequate internal controls to detect and prevent SARs from being entered into the system. In response to our report, FinCEN committed to implementing a corrective action plan by June 2003. Although concurring with the reported findings, FinCEN also claimed that the existing SAR data error rate had been well within acceptable limits.

From our initial follow-up audit work, we determined that FinCEN had made little progress in addressing the reported weaknesses or audit recommendations by the June 2003 timeframe. Moreover, we determined that FinCEN had not established data quality standards from which SARs could be routinely monitored for data quality purposes. What progress had been made in addressing our prior report consisted largely of additional outreach with financial institutions as to the proper filing of SARs. Little if any progress had been made to enhance internal controls to detect and prevent SARs with data quality problems from being entered onto the automated data system. (See Finding 1 on page 13.)

Given FinCEN's continued lack of systematic monitoring for SAR data quality problems, we expanded our audit work by reviewing a statistical sample of 406 SARs filed by depository institutions (DIs) and money services businesses (MSBs) over a twelve month period

¹ The BSA Advisory Group is a panel of experts that was established to advise the Treasury Department on ways to increase the utility to law enforcement of anti-laundering programs and eliminate unnecessary and over costly regulatory measures.

² In our December 2002 report, the problem of inaccurate and incomplete SAR data was actually reported as a repeat condition as first reported in *The Financial Crimes Enforcement Network Suspicious Activity Reporting System*, OIG-99-032, January 1999.

ending October 2003³. We met with four different federal law enforcement agencies (including case agents) and asked them to identify the types of SAR information that would be critical for (1) identifying potential investigative leads, and (2) developing trend analysis for such things as strategic planning and intelligence gathering. By focusing our review on these critical data fields, our intention was to avoid identifying trivial or minor technical SAR data quality problems.

We found that 251 (62%) of the 406 sampled SARs contained one or more data quality problems (i.e., missing, incomplete, inappropriate, and or inconsistent information) in a data field critical to law enforcement agencies. The problem SARs had been filed by 110 (68%) of the 161 filers in our sample. Based on the sample results, we estimate that approximately between 227,000 and 267,000 of the 416,000 SARs filed during the 12 month audit period contained similar errors as that observed from the 406 sampled SARs⁴. Our projections did not take into account the additional problems associated with the known level of duplicate filed SARs in the system. (See Finding 2 on page 15.)

In addition to measuring the *extent* of SAR data quality problems, we further analyzed the sampled SARs to gain a better understanding of the *nature* of problem SARs, such as whether there were discernable differences between depository institutions versus MSBs, and paper versus electronically filed SARs. We also isolated those data fields with the most frequent problems for further analysis. Some of our observations include: (1) although MSBs had more data quality problems than DIs, both groups had data quality problem rates in excess of 55%, (2) SARs filed electronically were not more accurate than paper filings, and (3) the most frequent type of data quality problem involved missing data that law enforcement would use to identify suspects for investigative purposes, and (4) a common problem with MSB SARs

³ At the time of our sample selection, depository institutions and MSBs collectively accounted for about 99% of all filed SARs over a 12 month period.

⁴ The statistical projections were made at the 95% confidence level and had a $\pm 4.7\%$ error rate.

entailed either missing or an inadequate narrative description of the suspicious activity. (See Finding 2 on page 18.)

Finally, we also looked at how timely SARs had been filed and processed to gauge how quickly law enforcement might gain access to SARs. We found that, on average, SARs with data quality problems took longer (73 versus 67 days) than non-problem SARs, as measured from the time of the suspicious activity to the time the SAR was entered onto the automated data system. In addition, just over 25 percent of the sampled SARs entailed total processing times exceeding 60 days. Most of the lapsed time could be accounted for by financial institutions' filing time rather than IRS processing time. (See Finding 2 on page 23.)

We believe that SAR data quality problems were due to various causes as we previously reported in December 2002. And our sampled SARs and follow-up discussions with financial institutions provided further insights. For example, we determined that for paper SARs, the IRS DCC contractor was only required to verify about a third of the data fields deemed as critical by law enforcement agencies. In addition, the continued absence of adequate internal controls to detect problem SARs and prevent them from being entered onto the SAR data system remains the primary weakness resulting in SAR data quality problems. (See Finding 3 on page 25.)

With 62% of the sampled SARs containing data quality problems, the OIG believes that this longstanding problem can not be construed as falling within acceptable limits, and needs FinCEN's heightened management attention. Unless sufficient progress is made in addressing this problem, the resulting adverse impact on law enforcement agencies will likely magnify as the number of different types of financial institutions become subject to the SAR filing regulation, as clearly shown by MSBs beginning in 2002. Even FinCEN's own BSA initiatives could be adversely impacted such as the new \$18 million BSA Direct system designed to expedite user access to and analysis of SAR data.

Before we issued the draft report, FinCEN provided us with a revised corrective action plan in response to our prior report of December 2002. We believe FinCEN's revised corrective action plan of September 2004 is an improvement over its predecessor version of July 2003. We also believe that if properly implemented, FinCEN's revised corrective action plan largely addresses our previously reported weaknesses and audit recommendations.

Nevertheless, based on our current audit findings gained from the 406 sampled SARs, we make 14 recommendations aimed at refining or enhancing various aspects to FinCEN's revised corrective action plan. Foremost is the need for FinCEN to officially designate a data integrity officer, and to establish data quality standards from which to systematically monitor SARs. (See Recommendations on page 29.)

Management Comments

In its comments to our January 19, 2005 draft report, FinCEN management stated that our recommendations, when considered contextually and accorded the appropriate priority in view of the many important compliance issues, will assist FinCEN in better ensuring that SARs contain as much useful information as is available to filers. This, according to FinCEN, will maximize the utility of the SARs to law enforcement and other consumers of the data. In its specific comments to the recommendations, FinCEN generally concurred with our recommendations and described the actions taken or planned in response to each recommendation.

FinCEN management emphasized its commitment to effective BSA implementation. However, FinCEN management believes that our report needs to be placed in context for two reasons. First, undue focus on data quality may skew the perspective of the filers and could undermine the overall effectiveness of financial institution SAR reporting programs by creating distorted incentives. Second, our report could be read to portray unfairly the level of industry compliance with the suspicious activity reporting rules. FinCEN

management also cited a concern that while our report acknowledges certain assumptions and inherent research limitations, these caveats to our report conclusions are not readily apparent.

According to FinCEN management, its approach to enhancing data quality is targeted toward education and outreach to the financial industry, combined with a periodic analysis of reports filed and the pursuit of appropriate remedial action against filers with systemic data quality issues. FinCEN has taken this approach in lieu of inflexible rules preventing SARs with blank or incomplete fields from being filed in the first instance. While it is seeking to enhance data perfection capabilities on the front end, FinCEN believes that it cannot risk a delay in an even imperfect report being placed in the database when it may be critical to law enforcement.

FinCEN management noted that in 2004, FinCEN expanded dramatically its role in the administration of the BSA, including creating a new office to support the examination function performed by other agencies and devoting one-third of its analytical resources to regulatory compliance support. This expansion – with an accompanying augmentation in resources – is expected to better identify and address SAR data quality problems.

FinCEN management provided a number of observations in its comments which are summarized below:

- The SAR is designed to provide law enforcement with lead information, not proven facts. FinCEN management expressed concern that this important perspective is lost in the report and that the report suggests a zero tolerance for errors or omissions.
- SAR data quality is but one of many important BSA compliance issues. As the delegated administrator of the BSA, FinCEN has an obligation to determine where it will devote resources to ensure effective BSA implementation. By focusing on a single aspect of compliance, FinCEN is concerned that it may well lead filers to do the same. While our report asserts that over half of

the SARs are problematic because one or more critical fields are blank or contain inappropriate information, it is impossible to assess whether those SARs are of less value to law enforcement on an aggregate basis.

- The conclusion that 62% of the suspicious activity reports filed contained data quality problems is potentially misleading. “Problem” SARs include those reports filed with a single field missing, such as the phone number of the suspect – such information may be difficult or impossible to obtain, and alone does not serve a foundation for concluding that the SAR is of little value. Whether a missing field affects the value of a SAR depends on the facts and circumstances – the impact cannot be quantified statistically.
- There may be legitimate reasons why certain information may not be provided in a SAR, such as when the filer does not have the information. Even with blank fields or fields containing inconsistent information, the narrative section provides critical analysis, and may provide more information to law enforcement than any other field. In this regard, FinCEN will continue to focus on ensuring that filers provide a comprehensive description in the narrative section.
- Our report does not provide the information necessary to determine whether a SAR was timely filed. The timeframe between the conclusion of the suspicious activity, as provided in the SAR, and the date the report was filed does not conclusively establish whether the SAR was filed in a timely manner because the date the activity was discovered is not reported. Moreover, FinCEN believes it essential that financial institutions use the allotted filing time to ensure that the facts are reviewed and the reports receive appropriate senior level review before they are filed.
- The criticism leveled against reports filed by MSBs must be measured against the realities of compliance in the industry. MSBs range from several large, highly sophisticated services

providers to a countless number of small “mom and pop” businesses that do not speak English. MSB industry compliance remains a central focus of FinCEN, but ensuring the implementation of the most basic of recordkeeping and reporting requirements continues to be a significant challenge. While FinCEN takes enforcement actions against MSBs when warranted, it will continue to focus resources on identifying these businesses and educating them on BSA regulatory requirements.

The complete text of FinCEN’s response is provided as Appendix 5.

OIG Evaluation

We believe that our report appropriately acknowledges the limitations and caveats cited by FinCEN above and we conducted our analysis in a manner to avoid identifying trivial or minor technical SAR data quality problems. Additionally, we considered whether SAR narratives included critical information that was omitted in the data fields. We also have not advocated a “zero tolerance” for SAR errors and omissions. And as FinCEN cites in its response to the draft report, the number of errors affecting the value of the SAR can not be gauged without knowing the facts and circumstances of the individual report. However, due to the absence of FinCEN data quality standards, we purposely avoided implying any level of tolerance for errors. In this regard, we would reiterate that a single field was a part of the collective information that law enforcement noted as being important in developing investigative leads and or for the purpose of identifying trends.

Our purpose in presenting filing and processing timeframes for the sampled SARs was to show when SAR information would be available to law enforcement, and for FinCEN to consider in ascertaining whether current regulatory timeframes are responsive to the needs of law enforcement. FinCEN is correct that it cannot be conclusively determined whether the institutions were late in filing the SARs as the regulatory filing timeframes are based on the date the institution first identifies the suspicious activity, which is

information not captured on the SAR form. We note this limitation in the report. However, as the report describes below, groups of SARs with lengthy timeframes far exceeding regulatory time frames does indicate potential regulatory non-compliance, and we believe FinCEN should monitor for such patterns.

Furthermore, we recognize the challenges faced by FinCEN with ensuring compliance by the MSB industry with SAR requirements. Our intent by providing data on the MSB SARs in our sample is to highlight the specific and unique problems found with the MSB filings so as to assist FinCEN in refining its outreach and enforcement efforts. For example, we noted that many MSB SARs either lacked any narrative descriptions of the suspicious activity or the narratives provided such little information that we believe they were of negligible value to law enforcement.

The extent of problem SARs found in our sample (62 percent) clearly warrants increased attention to SAR data quality. In this regard, we believe SARs continues to be a basic underpinning to many of FinCEN's BSA programs and mission. We also believe FinCEN's September 2004 revised corrective action plan to our December 2003 report and the corrective actions taken and planned in response to the recommendations in this report demonstrate a marked increase in FinCEN management's commitment and responsiveness to address SAR data quality issues.

Background

FinCEN's mission is to safeguard the U.S. financial systems from criminals and terrorists and to assist law enforcement in the detection, investigation, and disruption of illicit activity by administering the Bank Secrecy Act (BSA). A major aspect of this responsibility is the collection and maintenance of suspicious activity reports (SARs) that financial institutions are required to file

when they identify a suspected criminal activity, such as money laundering and terrorist financing.⁵

Under a 1996 joint agreement, the Internal Revenue Service (IRS) collects, processes, and stores SARs at its Detroit Computing Center (DCC). From the filed SARs, the IRS DCC creates and maintains a SAR database, known as the Suspicious Activity Reporting System (SAR System). SAR filers may choose from four media of filing: hardcopy paper, magnetic diskettes, magnetic cartridges, or an Internet medium known as the Patriot Act Communication System (PACS). Nearly 1.5 million SARs have been filed with FinCEN from April 1996 through December 2003.

Federal and State law enforcement agencies, as well as federal regulators for financial institutions, have access to the automated SAR System. SAR information is used for various functions, depending on the users authorized responsibilities. For example, law enforcement agencies may use SARs to investigate financial crimes, whereas financial institution regulators may use SARs to ensure industry compliance with the BSA.

The OIG has issued two reports dealing with the quality of SAR data. In a January 1999 report, we first reported on SAR accuracy problems involving SARs with missing information that law enforcement needed. More recently, in December 2002 we reported again that the same types of SAR data quality problems were still being identified by law enforcement agencies. Additionally, over 3,000 duplicate SARs were entered into the data base in the prior year. We noted this repeat audit finding and emphasized the need for enhanced controls to prevent and detect SARs with data quality problems from being entered into the SAR System.

FinCEN concurred with our December 2002 report and committed to addressing the reported weaknesses and recommendations, with a targeted completion date on most weaknesses by June 2003.

⁵ 31 CFR 103.17 - 103.21

Although committing to address this longstanding problem, FinCEN also noted that "...the current error rate is well within acceptable limits."

The events of September 11, 2001 intensified the importance of SARs in tracing financial crimes, as well as transactions used to finance terrorist activities. The USA PATRIOT Act passed shortly thereafter, extended BSA reporting requirements to other financial institutions such as insurance companies, securities brokers, and even gem dealers. The volume of SARs will likely increase significantly in future years, as demonstrated by the number of SARs filed by money service businesses beginning in January 2002.

Findings and Recommendations

Finding 1 Little Progress in Correcting Reported SAR Data Quality Problems

As noted above, we reported in December 2002 that FinCEN's SAR data quality problem was a recurring problem going back to 1999. In response to the December 2002 report, FinCEN committed to various corrective actions with a target completion date of June 2003, but claimed that the existing SAR error rate had been within acceptable limits.

We found that little if any substantive progress had been made toward addressing the December 2002 reported conditions or implementing the corrective actions. What corrective actions had been taken dealt largely with filer outreach as to proper SAR filing. Moreover, we found that FinCEN had not developed data quality standards from which SAR data quality could be monitored, and that there was no documented support or institutional recollection for the assertion that errors were within acceptable limits.

From our initial follow-up audit work completed by October 2003, we found that FinCEN's draft corrective action plan had attempted

to address our December 2002 report. The corrective action plan was drafted by July 2003 and provided for:

- Identifying and removing duplicate SARs filed in 2002;
- Emphasizing SAR data quality in industry outreach efforts;
- Expanding edit and validity checks;
- Establishing mandatory SAR fields, and corresponding with filers to obtain missing or corrected information in those fields;
- Identifying industry trends and specific filers with persistent errors.

We found that FinCEN had started implementing the outreach features of the corrective action plan, but the majority of control weaknesses and reported conditions remained outstanding. In addition, we believe the corrective action plan suffered from several omissions, and key aspects were premised on unreliable assumptions, casting doubt on whether the plan would effectively address SAR data quality problems. More specifically, we found that:

- The previously identified 3,000 plus duplicate SARs were still in the SAR System, and almost 4,000 duplicate SARs had been filed in the subsequent year.
- Plans to expand manual and system edit checks lacked supportable cost estimates. We were unable to evaluate the estimated costs due to the lack of sufficient details, supporting documentation, and material differences in cost estimates between FinCEN's and IRS' cost figures. Consequently, we were not able to assess the adequacy of the planned data quality control enhancements.
- Reliable cost estimates aside, FinCEN officials were also uncertain sufficient funding would be available.
- Mandatory fields for either monitoring or enforcement purposes had still not been established.
- Error rate standards from which to monitor data quality were not provided in the plan.

-
- Finally, the corrective action plan lacked an implementation schedule with target completion dates for each provision.

Given the lack of sufficient progress in addressing our December 2002 report, we expanded our audit field work to independently assess the extent of SAR data quality problems.

Finding 2

Extensive SAR Data Quality Problems Likely to Impact Law Enforcement Usage

Given FinCEN's lack of sufficient progress in addressing our prior report, we statistically sampled 406 SARs filed over a 12 month period for detailed review and analysis. To avoid focusing on minor and trivial data quality problems, we met with four different federal law enforcement agencies to identify those SAR data fields deemed to be critical for identifying investigative cases and or developing aggregate SAR trend analysis.

We found that 251 (62%) of the 406 sampled SARs contained a data quality problem in one or more critical SAR data fields. From the sample, we estimate that as many as 267,000 SARs filed over the year ending October 2003 may have similar data quality problems as the sampled SARs. Even though FinCEN had not actually established standards to systematically gauge data quality, we believe that our observed 62 percent data quality problem rate would likely exceed any measure of reasonableness, and is more accurately described as excessive.

Sample Selection and Basis for Identifying Data Quality Problems

From IRS records, we determined that about 416,000 SARs had been filed over a 12 month period ending October 31, 2003.⁶ From the total filings we statistically sampled 406 SARs, which were comprised of 203 filed by depository institutions (DIs) and

⁶ The total universe was adjusted for sampling purposes and excluded roughly 37,000 MSB SARs that would have omitted certain information. (See Appendix 1, on page 43.)

203 filed by money service businesses (MSBs).⁷ Other sample characteristics included 240 paper and 166 electronic filings, i.e., diskette, cartridges, or PACs.⁸ The 406 sampled SARs were filed by 161 different financial institutions.

To avoid focusing on data quality problems of a minor or trivial nature, we met with four different federal law enforcement agencies and asked about the critical data fields used to identify investigative leads to suspected financial crimes such as money laundering and terrorist financing. Some of the law enforcement agencies also aggregated SARs for other analysis, such as identifying emerging trends and patterns, resource deployment or policy initiative strategies, or to develop intelligence information.

Based on input from the law enforcement officials, including case agents, we focused our detailed review on about 50% of the available SAR data fields.⁹ These critical data fields were then reviewed for data quality problems defined as missing, incomplete, inappropriate, or inconsistent information.¹⁰ For example, errors might entail missing account numbers, filers marking the “other” suspected criminal activity designation with no further explanation, or the suspected criminal activity checked-off was inconsistent with the narrative explanation of the suspicious activity.

The *Extent* of SAR Data Quality Problems

From our detailed SAR reviews, we found that 251 (62%) of the 406 sampled SARs had missing, incomplete, inappropriate, and/or inconsistent information in one or more data fields deemed critical

⁷ As noted previously, DIs and MSBs accounted for 99% of total SARs. Filers not sampled included casinos, card clubs, and broker/security dealers.

⁸ Paper SARs accounted for about 53% of total SAR filings for the year.

⁹ The total number of data fields differed between the DI and MSB SAR forms.

¹⁰ SARs were not reviewed narrowly on the basis of the cited types of data problems. We did not count the SAR as a problem if it was obvious from the entire SAR that the missing, inconsistent or incomplete data fields could be reasonably explained. For example, certain missing suspect identification fields could be reasonably explained when the suspected crime involved non-account holders or other external parties.

to law enforcement agencies for either investigative or trend analysis. The problem SARs had been filed by 110 (68%) of the 161 financial institutions in the sample. The SAR data quality problems involved to varying degrees both investigative case development and aggregate trend analysis data fields, as shown in the following table.

Table 1
Extent of SAR Data Quality Problems

Data Quality Problems in:	Number of SARs with Data Quality Problems Affecting	
	Investigative Fields	Trend Analytic Fields
1-4 Fields	191 (47%)	153 (38%)
5-8 Fields	47 (12%)	14 (3%)
9-23 Fields	9 (2%)	1 (< 1%)
SARs with Problems (a)	247 (61%)	168 (41%)
SARs With No Problems	159 (39%)	238 (59%)
Total SAR Sample	406 (100%)	406 (100%)

Source: OIG Analysis

Note (a): The previously cited 251 total problem SARs was comprised of 247 problem SARs affecting investigative fields plus four SARs affecting only trends analytic fields. Most problem SARs affected both types of critical SAR data fields.

Based on the sample results, we estimated that the total number of SARs with similar data quality problems filed by DIs and MSBs during the 12 month period ranged from 227,000 to 267,000 SARs.

According to law enforcement officials, a problem SAR would not necessarily be useless in pursuing an investigative lead because the filing institution could be contacted for follow-up on a specific data field. However, follow-up for such purposes may add time to or delay the investigative process. Follow-up for such clarifications might also detract from other more potentially productive cases should subsequent follow-up yield non-productive information. One law enforcement agency indicated that there were so many SARs filed that they would simply ignore SARs with data problems and

continue culling through the remaining SARs until a sufficiently complete one could be used to assess the investigative potential.

The potential impact of data quality problems on law enforcement when developing aggregate trend analysis would likely be quite different than for investigative purposes. For trend analysis, aggregating data fields would be conducted without knowledge of specific problem data fields because the SAR System does not flag those SARs with missing, incomplete or inconsistent data fields. Some concerns include misleading trends, skewed indications of emerging financial crimes, and erroneous intelligence. Duplicate SARs and or missing information on the location of the suspicious criminal activity could also adversely impact resource deployment decisions and or policy initiatives.

The *Nature* of SAR Data Quality Problems

In further analyzing the 251 SARs with data quality problems, we found certain differences as well as similarities based on some of the sub-group sampling characteristics.

Type of Filing Financial Institution - Within their respective filing groups, both DIs and MSBs had high data quality problem rates (henceforth defined as the number of SARs with data quality problems divided by the total number of reviewed SARs), but data quality problems were clearly higher for MSBs than for DIs as shown below.

Table 2
SAR Data Quality Problems for MSBs vs. DIs

	MSBs	DIs
Problem SARs	138 (68%)	113 (56%)
SARs – No Problems	65 (32%)	90 (44%)
Totals	203 (100%)	203 (100%)

Source: OIG Analysis

Although not reflected in the table above, we found that three MSBs accounted for the majority of the problem MSB SARs. These three MSBs accounted for 106 (77%) of the 138 problematic MSB SARs. We also found that MSB problem SARs generally had a greater number of problem data fields per SAR than DIs. For example, 34 MSB SARs had between 5 and 8 problem data fields, as compared to 13 DI SARs with a comparable level of problems; see Appendix 2 for a further detailed breakout. Also see Appendix 3 for our projected number of SARs with data quality problems for MSBs versus DIs for the year.

Filing Medium - We found a 5 percent difference in the data quality problem rate between paper and electronically filed SARs as shown below.

Table 3
SAR Data Quality Problems Paper vs. Electronic Filings

	Paper	Electronic
Problem SARs	143 (60%)	108 (65%)
SARs – No Problems	97 (40%)	58 (35%)
Totals	240 (100%)	166 (100%)

Source: OIG Analysis

We did not assess if the 5 percent difference was statistically significant or project this difference beyond the sample. Although not shown in the above table, MSBs accounted for a majority (60%) of the paper SARs with data quality problems.

Most Problematic Data Fields – Of the 251 SARs with data quality problems, we found that the most problematic data fields were largely related to the suspect's identity or whereabouts, as shown in the following table.

Table 4
Most Problematic SAR Data Fields

SAR Data Fields With Problem	Number of SARs	(%) of Sample
SSN, EIN, or TIN	64	16
Date of Birth	65	16
Phone number	82	20
State of Subject	22	5
Street Address of Subject	26	6
Zip Code of Subject	23	6

Source: OIG Analysis

According to law enforcement officials, not only are these types of data fields critical in pursuing investigative leads, but it was their belief that these were the fields with the most common data quality problems. For example, the date of birth was mentioned as a problematic data field. As one law enforcement official emphasized, numerous individuals may have identical names, so the subject's name is of less value unless accompanied by the date of birth.

Data Fields Particularly Problematic with MSBs - We found that 77 (38%) of the 203 MSB SARs had a problem with the narrative field in terms of adequately describing the suspected criminal activity. In contrast, less than 5% of the sampled DI SARs had this type of problem. The narrative section is to provide a detailed description of the events that led to filing a SAR, and is considered critical by most of the law enforcement officials we met.

Of these 77 MSB problem SARs, 14 failed to include a narrative description. Many of the remaining problem narratives contained so little information that we believe they would have been of negligible value to law enforcement. Illustrating this problem is one MSB SAR with the following description, "Funds transfer transactions purchased in patterns to indicate suspicious activity."

One or two sentence narratives such as this were typical of these problem MSB SARs.

The phone number of the business where the suspicious activity occurred was another common yet fundamental problem with MSB SARs. This data field was either missing or incomplete for 35% of the sampled MSB SARs. The data field is fundamental to law enforcement in following-up with the MSB to clarify missing, incomplete, inappropriate, or inconsistent information.

We also observed that suspect identification information was not included in 52 (25%) of the 203 sampled MSB SARs. All 52 SARs reported a suspected money laundering technique known as transaction structuring.¹¹ However, because the individual transaction amounts reported were under \$3,000, the filer was exempt under the BSA regulations from recording customer identification information.^{12 13}

Most Frequent Types of Data Quality Problems - By far the most frequent type of data quality problem was missing information. Missing information in the investigative critical data fields was a problem in 185 (46%) of the 406 sampled SARs. By comparison, 110 SARs (27%) had missing data in fields critical for trend analysis. The frequency for each type of data quality problem affecting investigative and trend critical data fields is shown below.

¹¹ Structuring refers to the act of completing a series of sequential transactions for the purpose of disguising the ultimate beneficial owner and or originating source of the transaction.

¹² Due to the \$3,000 exemption, the 247 problem SARs reflected in Table 1 excludes 18 of the 52 MSB SARs mentioned above. The other 34 SARs were included in the 247 because they had other types of data problems.

¹³ During our audit, we discussed the \$3,000 threshold for requiring institutions to record customer identification information for funds transfers and money orders with FinCEN. A FinCEN official told us that this threshold is currently being reevaluated by the BSA Advisory Group. This reevaluation includes FinCEN's plans to solicit comments via a questionnaire expected to be published in 2005.

Table 5
Frequency of the Types of SAR Data Quality Problems

Type of Data Quality Problem	Problem SARs Affecting		Percent of Sample	
	Investigative Fields	Trend Analysis	Investigative Fields	Trend Analysis
Missing Information	185	110	46	27
Missing From Field, But in Narrative	See note	21	See note	5
Inappropriate Info	107	78	27	19
Incomplete Info	55	13	14	3
Inconsistent Info	7	3	2	< 1

Source: OIG Analysis

Note: We did not categorize as a problem SAR "Missing From Field, But in Narrative" as affecting the investigative fields because the information was still provided. However, for trend analysis these SARs are considered problematic because any analysis performed on a blank field could be materially impacted by the missing information.

Duplicate SARs Filed

Our December 2002 report noted that the SAR System contained over 3,000 duplicate SARs identified for the year 2001. During our initial follow-up field work, IRS personnel identified about 7,300 duplicate SARs posted to the SAR System in calendar years 2001 and 2002.

In July 2004, we were advised by a senior FinCEN official that these duplicates had still not been purged from the SAR System nor were they marked for ease of identification for SAR users. More recently, we were again advised that the SAR System was canvassed again, and for the period 1996 through 2003 about 1% of the SARs were duplicates. We estimate that this would amount to roughly over 15,000 SARs.

Clearly, duplicate SARs could adversely impact law enforcement efforts when aggregating SARs to identify trends, assess resource deployment strategies, or formulate policy initiatives. FinCEN has acknowledged as much in congressional testimony, "...we are also

devoting analysts to study Bank Secrecy Act data and all other available information to gain an increased understanding of methodologies, typologies, geographic patterns of activity and systemic vulnerabilities relating to terrorist financing. These analysts will focus on regional and systemic 'hot spots' for terrorist financing, studying and analyzing all sources of information."¹⁴

In light of how SARs are being aggregated, we believe 15,000 duplicate SARs could materially skew law enforcement analysis, unless the extent and nature of duplicate SARs is systematically monitored.

Timeliness of SAR Filings and Processing

Besides reviewing the 406 SARs for data quality problems, we also looked at how long it took financial institutions to file and the IRS to process SARs onto the automated system. These timeframes taken together approximated how long before law enforcement would have access to SARs through the SAR automated data system.¹⁵

Under the SAR regulations, financial institutions are required to file a SAR within 30 days of discovery of the suspicious activity. DIs are given an additional 30 days if they are unable to identify a suspect. As shown below, we found from the sampled SARs it took on average 71 days between the day of the suspicious activity to the date the SAR was posted to the SAR System.

¹⁴ Testimony Before House Committee on Financial Services, Subcommittee on Oversight and Investigations, June 9, 2004

¹⁵ The OIG acknowledges the timeframe analysis does not take into account instances when financial institutions contact law enforcement directly in concert with filing the SAR.

Table 6
SAR Filing and Processing Timeframes

	Date of Suspected Activity To SAR Preparation	SAR Preparation To IRS DCC Receipt	IRS DCC Receipt To SAR System Posting	Total Elapsed Time
Total Sample Average (a)	53	12	7	71 (b)
Paper SARs	48	15	10	72
Electronic SARs	59	7	3	69
DI SARs	51	11	7	68
MSB SARs	54	13	8	73
SARs With Data Problems	56	12	7	73
SARs Without Data Problems	47	12	8	67

Source: OIG Analysis

Note (a): Sample was reduced by 12 due to missing information needed to measure all the timeframes.

Note (b): Individual timeframes can not be added to derive the total elapsed time due to rounding and adjustments associated with missing date information.

Most of the total elapsed time can be accounted for by the filing institution rather than IRS processing time. As shown in the above table, IRS processing time was the shortest average time of the four measured timeframes.

Total elapsed time differed very little between paper and electronic filings (72 versus 69 days), but it appears to take financial institutions longer to prepare the SAR when using an electronic media (59 versus 48 days).

The largest difference in elapsed time was between SARs with and without data quality problems. The former took on average 6 more days before getting into the SAR System.

Though the total elapsed time averaged 71 days, there were 154 SARs (52 DIs and 102 MSBs), or 38%, that may have exceeded applicable regulatory SAR filing timeframes, as shown below.

Table 7
Comparing MSB & DI SAR Filing Timeframes
(Suspected Activity to IRS DCC Receipt)

Days Elapsed	Number of SARs				Total Sample
	DI		MSB		
0-30	110		99		209 (52%)
31-60	39		46		85 (21%)
61-90	22	} 52	27	} 102	49 (12%)
91-120	9		6		15 (3%)
121-1,383	21		23		44 (11%)
Totals	201		201		402 (99%)

Source: OIG Analysis

Note, DIs are given an additional 30 days to identify a suspect, whereas MSBs are not accorded the additional 30 days. As shown above, 52 DIs total filing time exceeded 60 days, whereas almost twice as many MSBs (102) exceeded 30 days. Because we were not able to determine when the filer had first suspected a potential violation (i.e., the discovery date), the above table only provides an indication of potential late filings. Of particular note would be the 44 SARs with total filing times exceeding 120 days or four months.

Finding 3

Causes and Factors Contributing to SAR Data Quality Problems

We noted in Finding 2 that 62% of the sampled SARs had missing, incomplete, inappropriate, or inconsistent data in at least one data field deemed to be critical to law enforcement agencies. Our prior December 2002 report attributed various causes and factors for the SAR data quality problems. While our sampled SARs illustrated the extent of data quality problems, our analysis of the nature of those problems surfaced additional causes and contributing factors that we had not previously identified. Discussions with 15 SAR filers also provided additional insights. These causes and contributing factors can be grouped into four categories: (1) overall system controls, (2) broad reliance on financial supervisory

regulators, and factors unique to either (3) the type of filer or (4) filing medium.

Absence of Overall Controls to Detect and Prevent SARs with Data Quality Problems – As noted in Finding 1, FinCEN had not implemented our prior recommendation to establish system controls to screen and prevent SARs with data quality problems from being entered onto the SAR System. We believe this situation continues to be a primary cause and management weakness. The lack of adequate controls is illustrated by the following:

- FinCEN had not created a position either internally or at the IRS DCC with specific responsibility for monitoring for and ensuring SAR data quality (i.e. a Data Integrity Officer). Instead, monitoring was largely done sporadically on an ad hoc basis.
- FinCEN had not established data quality standards to routinely monitor and measure performance. IRS did, however, have limited error rate standards for the contractor who transcribed paper SARs into an electronic format for uploading onto the SAR System. However, these contractor standards only covered paper filings, were not comprehensive, and were in need of refinement, as discussed further below.
- The SAR System was not routinely screened for duplicate filings. Thus duplicates were not purged or flagged so that law enforcement users could systematically make any needed adjustments when aggregating SAR data for trend analysis.
- Electronically filed SARs were not subject to system edits or data perfection routines other than for format.
- There was no systematic program or process for corresponding with filers for known problems. Consequently, FinCEN lacked a systematic mechanism to provide filers with feedback on any problem SARs they specifically filed.

-
- No systematic mechanism existed for obtaining law enforcement feedback or input specifically dealing with data quality. According to one senior member of the BSA Advisory Group, and from a review of recent meeting minutes, SAR data quality has not been an agenda item, nor has law enforcement agencies been routinely contacted to identify critical SAR data fields prior to our audit.

Instead of enhanced detection and prevention controls, FinCEN appears to have focused primarily on industry outreach. For example, FinCEN made Frequently Asked Questions and clarifying guidance available on a website, revised filing instructions, and covered additional filing guidance tips in their periodic *The SAR Activity Review, Trends, Tips and Issues* reports. The singular focus of outreach in lieu of enhanced system controls over problem SARs may have reached a marginal level of effectiveness, in light of our observed SAR data quality problem rate of 56% for DIs (which have been subject to SAR filing since 1996). Furthermore, 14 of the 15 institutions we contacted attributed problem SARs to filer error and oversight.

Broad Reliance Placed on Financial Supervisory Regulators – FinCEN does not have in-house staff to examine financial institutions to ensure compliance with the BSA. Instead, FinCEN relies on the federal functional regulators to ensure that SARs are complete and accurate. Through onsite examinations, these federal regulators check for compliance with the various requirements of the BSA, including SAR filing.

From a review of the regulators' examination handbooks, we found that these examination procedures may not be complete or even provide for addressing whether an institution files accurate and complete SARs. Of the six regulators responsible for examining DIs or MSBs for BSA compliance, we found that only two examination handbooks specifically provided for assessing the completeness and accuracy of SARs. However, these two handbooks lacked guidance or criteria as to how these assessments were to be completed or what even constituted a

complete and accurate SAR. The other four regulators focused only on whether financial institutions were filing SARs when warranted. All six handbooks lacked any discussion as to specific SAR data fields as being critical or vital to law enforcement needs.

The absence of specific examination guidance addressing SAR accuracy and completeness was reflected in our sampled SARs. We sorted the 251 SARs with data quality problems according to the filing institution's primary regulator, and then compared the data quality problem rates. In relative percentage terms, no single regulator appeared to have been highly effective in ensuring their respective institutions filed accurate and complete SARs as shown below.

Table 8
SARs with Data Quality Problems Sorted by Regulator

Regulator	Problem SARs	Total Sampled SARs	SAR Problem Rates (%)
OTS	13	17	76
NCUA	9	12	75
IRS	138	203	68
FDIC	21	38	55
OCC	56	107	52
FRB	14	29	48
Totals	251	406	62

Source: OIG Analysis

Note, the IRS' SAR totals include Postal Service filings.

MSB Outreach Did Not Focus on Completeness and Accuracy – We noted in Finding 2 that MSBs had a higher SAR data quality problem rate than DIs (68% versus 56%). Based on discussions with officials and review of various documents, we found that FinCEN's initial SAR outreach material to the MSB industry was not provided until May 2003, 16 months after the industry had been subject to SAR filing in January 2002. Furthermore, the initial material that was sent to about 640 MSBs did not specifically

cover the topic of filing complete and accurate SARs. Instead, the material only covered the filing requirement.

SAR Data Quality Problems Unique to Paper Filings – In our December 2002 report, we noted that one cause of problems entailed data entry problems arising from the transcription of paper SAR information into an electronic format by a contractor for the IRS. The contractor is subject to a quality assurance process whereby certain data fields are to be keystroke verified. This entails entering certain data fields twice and resolving any differences. To test the accuracy of the contractor's data transcriptions, we compared the originally filed paper SARs in our sample to the SAR record in the automated system.

From our audit tests along with discussions with IRS officials and a contractor representative, we determined that:

- Less than one-third of the data fields deemed by law enforcement as being critical for investigations and trend analysis were subject to keystroke verification procedures covered in the contract.
- 40 (17%) of the 240 sampled paper SARs included keystroke errors.

Although the 17% keystroke error rate appears high, it should be noted that the contractor met one of the two contract quality standards. The contract provides for a 1% error rate standard for just those fields subject to the double keystroke verification procedures, and a 3% standard for essentially all other fields. Although the two standards are measured differently, we found that the contractor met the 1% standard but exceeded the 3% standard by about 14%.

Recommendations

Before we issued our draft report, FinCEN provided us with a revised corrective action plan in response to the December 2002 report. (See Appendix 4 on page 49.) We believe FinCEN's

revised corrective action plan, dated September 3, 2004, is an improvement over its predecessor version in July 2003. Based on our current findings and insights gained from the 406 sampled SARs, we are making the following recommendations aimed at refining and or enhancing various aspects to FinCEN's revised corrective action plan. We also include several recommendations to address weaknesses that were not identified in our 2002 report, or not addressed in the revised corrective action plan.¹⁶

Overall System Controls

In Finding 3, we noted that a primary cause for SAR data quality problems was a lack of an overall system of controls to better detect and prevent data quality problems. We believe that FinCEN's revised corrective action plan essentially addresses this weakness in terms of enhanced outreach, and quarterly identification of duplicates and SARs with blank fields. It also provides several means for resolving data quality problems, including referrals to bank regulatory agencies, direct follow-up with egregious filers, and remedial enforcement action, as necessary.

To enhance the revised corrective action plan, we recommend the following refinements:

1. Given the results of our sample, establish a position for a BSA data administrator (i.e., data integrity officer) with specific responsibility for ensuring the accuracy and timeliness of the SAR data system, or assign this responsibility to an existing position. We believe this would enhance both accountability and FinCEN's responsiveness to SAR users, filers, and regulators. We also believe this position would be better situated by

¹⁶ It should be noted that the OIG recalculated the overall error rate for the 406 sampled SARs using the 9 critical fields noted in the revised September 2004 corrective action plan. FinCEN's reduced data fields resulted in a 43% error rate. As the revised action plan points out, the process of determining the scope of critical fields is iterative.

reporting directly to FinCEN rather than the IRS.

Management Response FinCEN concurred with comment. It agreed with the concept of ensuring appropriate attention is given to BSA data integrity and for improving data quality through reasonable means, and that appropriate officials should be held accountable. Given its organizational and management structure, it will assign this responsibility and accountability to three existing Assistant Directors rather than a single individual. The target date for completion is April 31, 2005.

OIG Comments The OIG believes there could be added challenges to shared as opposed to singular accountability for data quality issues, and FinCEN should monitor whether this approach is effective. Nevertheless, we believe that FinCEN's planned management corrective action adequately addresses the intent of the recommendation.

In Finding 3, we pointed out that FinCEN had not established standards by which data quality would be monitored, and performance measured. The revised corrective action plan calls for quarterly automated reviews to identify filers with systematic or pervasive filings of duplicate SARs, or SARs with blank data fields. However, there is no specific mention of establishing standards for these reviews. Accordingly, so as to better ensure that such reviews are consistent and filers have a more precise understanding of what is expected, we recommend that the Director of FinCEN:

2. Establish measurable standards to address at least two data quality aspects: critical data fields that are responsive to law enforcement needs, and an acceptable *level* of data quality.

Management Response FinCEN concurred with comment. It plans to establish measurable standards to

address both critical data fields and acceptable data quality levels. In terms of critical data fields, FinCEN noted that it would expand obtaining input beyond law enforcement to include other SAR users such as federal regulators as well as SAR filers. FinCEN also commented that the identification of critical fields must be made in a manner consistent with its policy goals and objectives for the suspicious activity reporting regime, with an understanding that blank fields may be unavoidable or justifiable. In terms of acceptable data quality levels, FinCEN plans to establish criteria to be used during the planned quarterly analysis (as provided in the revised corrective action plan of September 2004) once they have established baseline data on the revised critical data fields. The target date for completion is December 1, 2005.

OIG Comments The OIG did not intend to limit obtaining input to law enforcement and believes FinCEN's plan to expand the process to other SAR users is commendable. However, the expanded process may present FinCEN with added challenges given users different authorities and responsibilities as noted on page 12. For example, FinCEN may find it necessary to establish several groups of "critical data fields" for assessing regulatory compliance as opposed to developing criminal investigative leads. Nevertheless, the OIG believes FinCEN's planned management corrective action adequately address the intent of the recommendation if properly implemented.

FinCEN's revised action plan of September 2004 suggests that periodic consultations have begun with the law enforcement liaisons. However, the plan is silent as to whether this is to be a continual evaluation. Based on our law enforcement contacts in identifying critical data fields, we would further recommend as a refinement that the Director of FinCEN:

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3. Establish a process to periodically include input from law enforcement case agents for a contemporary investigative perspective.

Management Response FinCEN concurred with comment. It plans to seek input not only from law enforcement, but also from filing institutions as well as the regulators. FinCEN noted that in addition to consultations with law enforcement liaisons, it currently seeks input from these sources at least every 3 years during the form renewal process, and more frequently when forms are amended. FinCEN, however, will establish a procedure for the periodic solicitation of additional input. The target date for completion is September 30, 2005.

OIG Comments The OIG believes FinCEN's planned management corrective action adequately meets the intent of the recommendation if properly implemented.

In Finding 2, we noted that there were about 15,000 duplicate SARs in the data system. FinCEN's revised corrective action plan addresses this problem with a plan to scan the SAR System quarterly, expanding outreach, and evaluating options for alerting SAR users of possible duplicates. As an added refinement, we recommend that the Director of FinCEN:

4. Assess the need to identify the specific data fields associated with the 15,000 duplicates and advise law enforcement so that they may better gauge the potential impact of duplicates. Duplicate SARs involving certain crimes may be of more importance to certain law enforcement agencies given their differing authorities over certain crimes such as credit card fraud versus mortgage loan fraud.

Management Response FinCEN concurs and plans to sample duplicate records to assess whether the

duplicates may affect statistical summaries of the SAR data. The target date for completion is September 30, 2005.

OIG Comments The OIG believes FinCEN's planned management corrective action adequately addresses the intent of the recommendation if properly implemented.

5. Assess the need and feasibility of identifying, tagging or segregating duplicate SAR filings into a suspense file until a more systematic process can be developed to prevent them from being entered into the system.

Management Response FinCEN concurred and stated that, given duplicates comprise a small fraction of the overall reports in the database, it will focus on education and outreach. FinCEN plans to identify on a quarterly basis, filers with systemic and pervasive duplicate filings, and to take appropriate action in reaching out to such filers. FinCEN further stated that within the current system it was not feasible to identify and segregate duplicate SARs. However, FinCEN will explore new technology to flag duplicate reports in its BSA data repository project, BSA Direct, which is currently under development.

OIG Comments The OIG believes FinCEN's planned management corrective action addresses the intent of the recommendation. We also believe this corrective action in concert with that in response to recommendation 3 will also provide SAR users an avenue to express the need for any further interim measures prior to the full implementation of the new BSA Direct system to flag duplicate SARs. The OIG also would agree in that in nominal terms duplicates may in fact be a small portion of total filed SARs. As noted on page 22, duplicates amounted to roughly 1 percent of all filed SARs. However, as noted in

Finding 2, duplicate SARs could materially skew law enforcement analysis, unless the extent and nature of duplicate SARs is systematically monitored.

In Finding 2, we provided information on the average filing and processing times for the sampled SARs. With just over 25% of SARs exceeding 60 days, and 11% taking longer than 4 months, we recommend that the Director of FinCEN:

6. Advise and solicit the views of law enforcement agencies as to whether the observed timeframes are responsive to their needs. In so doing, FinCEN will be better positioned to assess any needed changes, such as whether filer outreach or supervisory oversight should be focusing on the timely filing of SARs.

Management Response FinCEN concurred. It plans to solicit the views of law enforcement as well as the views of the federal regulators that supervise these institutions. FinCEN noted that the timeframes observed in the report alone do not indicate that its regulations were violated. The target date for completion is December 1, 2005.

OIG Comments The OIG believes FinCEN's planned management corrective action adequately addresses the recommendation if properly implemented. And as we noted in Finding 2, the reported timeframes are intended to bring to FinCEN's attention to indications of potentially late filings that we believe FinCEN should monitor.

7. Assess the need to review timeliness as part of the planned quarterly SAR reviews for indications of potential violations of the regulatory filing timeframes.

Management Response FinCEN concurred and plans to assess the feasibility of identifying institutions that may

be pervasively filing SARs after the required regulatory filing timeframes. If accurate information can be extracted, procedures will be developed for incorporating this data as part of the planned quarterly reviews. The target date for completion is September 30, 2005.

OIG Comments The OIG believes FinCEN's planned management corrective action adequately addresses the recommendation if properly implemented.

Although our analysis surfaced indications that as many as 154 SARs exceeded the 30 or 60 day regulatory timeframe, our analysis did not include a review of the filers' records to establish when the suspicious activities were discovered. We also did not determine whether any of the extensive filing timeframes were willful or due to negligence, and we did not assess whether any one filer demonstrated a pattern or practice of untimely filings. Nevertheless, we recommend that the Director of FinCEN:

8. Assess the need to refer any of the identified lengthy filing timeframes (those exceeding 30 or 60 days) to the applicable regulatory agencies to determine whether timely SAR filing is an area warranting detailed examination or enforcement action.

Management Response FinCEN concurred. If feasible pursuant to recommendation 7, FinCEN plans to refer financial institutions with pervasive filing deficiencies to the applicable regulatory agency for possible follow-up action. The target date for completion is December 1, 2005.

OIG Comments The OIG believes FinCEN's planned management corrective action adequately addresses the intent of the recommendation if properly implemented. The OIG also recognizes the difficulty of obtaining precise information to assess compliance with the

required filing timeframes given that the date the suspicious activity was discovered is not captured on the SAR form. However, as we note in Finding 2, the overall timeframes as measured from information available on the SAR form does provide an indicator of potential late filers. For example, total filing time for 44 (11%) of the 402 sampled SARs exceeded 120 days, well over the maximum 60 days accorded DIs under the regulation. Accordingly, we believe such large time periods as these provide a reasonable indicator of potential late filings worthy of follow-up.

Reliance on Financial Regulators

In Finding 3 we pointed out that the supervisory regulatory agencies responsible for examining financial institutions lacked clear guidance or procedures for examiners to assess SAR accuracy and completeness. We are aware of FinCEN's July 2004 initiative to establish the "Office of Compliance," charged with supporting the examination functions performed by financial regulators. Accordingly, we recommend that the Director of FinCEN ensure that the Office of Compliance:

9. Assesses the adequacy and consistency of regulators' examination handbooks covering financial institutions' compliance with the BSA SAR filing requirements. This assessment should include the need to clearly spell out examiners responsibilities, and the examination procedures to determine whether institutions are filing accurate, complete, and timely SARs.

Management Response FinCEN concurred. FinCEN is currently working with the five Federal banking agencies to draft interagency Bank Secrecy/Anti-Money Laundering examination procedures. At its request, guidance on SAR quality was added to the draft examination manual, including an examination procedure which directs examiners to sample reports filed by the

subject institutions. FinCEN has also started a similar process with IRS for their BSA examinations of money service businesses.

OIG Comments The OIG believes the management corrective action adequately addresses the recommendation if properly implemented.

FinCEN's revised corrective action plan also provides for notifying federal regulators of filers with systemic or pervasive duplicates and missing information for follow-up purposes. So as to better ensure timely follow-up in such cases, we recommend that the Director of FinCEN ensures that the Office of Compliance:

10. Establishes policies and procedures for timely routine follow-up on regulatory referrals to federal regulators to determine their supervisory resolution.¹⁷

Management Response FinCEN concurred. It plans to establish routine follow-up on referrals to regulators as a function of the newly created Office of Compliance. The target date for completion is December 1, 2005.

OIG Comments The OIG believes FinCEN's planned management corrective action adequately addresses the intent of the recommendation if properly implemented.

¹⁷ It should be noted that regulators may not act on a referral in a timely manner if they do not address the referral before the next scheduled exam. For example, some regulators' examination cycles range between 12 and 36 months before the next scheduled examination. Existing resources at one regulatory agency may preclude reexamination before 20 or more years. At the exit conference, however, FinCEN indicated that they could not request an expedited out-of-cycle examination of all the regulators to address a FinCEN referral.

Unique MSB SAR Data Quality Problems

In Finding 2 and 3 we noted several unique aspects to the problem SARs filed by MSBs. Accordingly, we recommend that the Director of FinCEN:

11. Assess the need for either enhanced outreach or supervisory enforcement action with the three MSBs accounting for over 77% of the problem MSB SARs in our sample.

Management Response FinCEN concurred and has assessed the issue, engaged in enhanced outreach, and taken appropriate regulatory action against these entities. The enhanced compliance activities have been completed in conjunction with pending or completed enforcement actions.

OIG Comments The OIG believes FinCEN's management corrective action adequately addresses the recommendation.

Unique Paper SAR Data Quality Problems

In Finding 3, we noted that the IRS DCC data transcription contractor for paper SARs was keystroke verifying data fields for less than a third of the data fields deemed critical by law enforcement agencies. Furthermore, 17% of our sampled paper SARs included keystroke errors. We recommend that the Director of FinCEN, in consultation with the IRS and law enforcement agencies:

12. Assess the need to expand the number of data fields subject to keystroke verification to include data fields critical to law enforcement.

Management Response FinCEN concurred. It plans to review the IRS SAR data entry contract and the

standards outlined for keystroke verification, as well as request copies of reports used by the IRS to ensure contractor adherence to the requirements. FinCEN noted, however, that keystroke verification will only result in correction of typos not in the addition of information that is available to the keyer. The target date for completion is December 30, 2005.

OIG Comments The OIG believes FinCEN's planned management corrective action adequately addresses the recommendation if properly implemented. We would also agree that key stroke verification would not address missing information. However, as a point of clarification, the recommendation is only intended to expand the number of data fields subject to keystroke verification to those deemed critical by SAR users.

13. Reassess how the contractor's 3% performance standard is to be measured so as to give greater consideration to the number of SARs with errors rather than just the total number of errors. This would provide added perspective to situations where a few SARs account for a large number of errors as opposed to a large number of SARs each with a few errors.

Management Response FinCEN concurred. It plans to establish a process to periodically obtain input from IRS as to how the 3% error rate is monitored and the number SARS involved. The target completion date is October 31, 2005. FinCEN also noted that, given the volume of reports processed by the IRS-DCC, the timeframes for posting SARs were very reasonable.

OIG Comments The OIG believes the planned management corrective action adequately addresses the intent of the recommendation if properly implemented.

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14. Assess whether the scope of the contract could be economically and feasibly expanded to identify SARs with missing and or incomplete data fields. This might provide FinCEN with a means of identifying egregious problem filers in a timelier manner than the quarterly reviews noted in the revised corrective action plan. This would also cover the majority of SARs since most SARs are filed by paper.

Management Response FinCEN concurred in concept. It has assessed a number of options to identify SARs with missing and incomplete data fields and determined that using information technology to identify records needing further analysis is the most cost effective approach. FinCEN has begun a process to receive computer-generated reports quarterly with highlights to certain types of data quality issues. According to FinCEN, the longer-term technology solutions include its BSA Direct project and accelerating electronic filing. A key design feature of BSA Direct project is the use of sophisticated data cleansing techniques that will automatically elucidate certain problems and dramatically improve the overall quality of the BSA data. BSA Direct will be operational in October 2005 so it is impractical to implement other temporary measures at this time. FinCEN also noted that there is a growing number of paper filers using its BSA E-Filing system to file their SARs.

OIG Comments The OIG believes FinCEN's management corrective action adequately addresses the intent of the recommendation.

* * * * *

We would like to extend our appreciation to both FinCEN and the IRS for their cooperation and courtesies extended to our audit staff during the audit. If you have any questions, please contact me at (415) 977-8810 ext. 222 or Jack Gilley, Acting Audit Manager, at (415) 977-8810 ext. 235. Major contributors to the report are listed in Appendix 6.

/s/

Benny W. Lee

Director, Western Field Audit Office

Appendix 1

Objectives, Scope and Methodology

Our audit objective was to assess the status of FinCEN's management corrective action plan in response to our December 2002 audit report. Our prior report disclosed problems with the completeness and accuracy of SAR records, and the existence of numerous duplicate SARs.

To assess FinCEN's implementation of our audit recommendations, we visited FinCEN in July 2003. Because SARs are collected at the IRS DCC, and the SAR data base is maintained by the IRS, we also visited the IRS DCC in August 2003. To assess the adequacy of FinCEN's corrective action plan, we interviewed FinCEN and IRS officials to determine the target dates for implementing the plan, the estimated cost of implementation, the basis for the cost estimates, the existence of obstacles to implementation, and whether FinCEN had formally requested the IRS to implement plan modifications.

We briefed FinCEN officials in October 2003 on our preliminary observations as to the little progress in implementing their management corrective action plan noted in their response to our December 2002 report. As a result, we expanded our scope to include detailed testing of a statistical sample of SARs to assess the accuracy and completeness of the database. Additional follow-up audit work was also conducted to assess the current level of duplicate SAR filings in the database.

Sampling Methodology

So as to avoid identifying SAR data quality problems of a technical and trivial nature, we met with law enforcement officials, including case agents, at the FBI, Secret Service, Department of Justice, and Department of Homeland Security. These officials included two members of the BSA Advisory Group, as well as the FBI and Secret Service FinCEN liaisons. We inquired about their use of SARs and any data integrity problems they had encountered, and what SAR data fields they considered critical for investigative case development and trend analysis.

Appendix 1

Objectives, Scope and Methodology

We conducted detailed SAR testing at the IRS DCC from December 2003 through February 2004. From IRS records, we determined that over 99 percent of SAR filings were made by depository institutions (DIs) and money services businesses (MSBs). Approximately 450,000 SARs had been filed by these two types of institutions over the 12 month period ending October 2003. We did not include SARs filed by securities and futures dealers, or casinos and card clubs in our tests, because they only comprised about 1 percent of the total SAR universe. This was the most current available information at the time of our sample.

The universe of over 450,000 SARs was adjusted by excluding about 37,000 MSB SARs with reported transactions of under \$3,000. This was to avoid inclusion of SARs where the filer was not required by regulation to obtain customer identification information.

From the resulting adjusted universe of about 416,000 SARs, we randomly sampled 406 SARs comprised of 203 SARs filed by DIs and 203 SARs filed by MSBs. Based on a predicted error rate of 5 percent, we determined the sample size to obtain a sample precision of ± 3 percent at a 95 percent confidence level. Our projections of problem SARs were based on the adjusted universe. We calculated the sampling error at a 95 percent confidence level based on the sample results.

We stratified our sample by media of filing so as to assess any differences between paper versus electronic filings. The latter consisted of diskette, cartridge, and PACS Internet.

In certain instances, we replaced a SAR in our sample with another randomly selected SAR. This was done, for example, if the SAR filer used an incorrect SAR form (e.g., an MSB used the SAR form for a DI).

Detailed SAR Testing Methodology

We reviewed each sampled SAR to determine if information in critical fields was complete, appropriate, and consistent. We did

Appendix 1

Objectives, Scope and Methodology

not attempt to reconcile sampled SARs with the filing institution's records.

We considered a SAR field as missing information if the field was blank, and incomplete if it was partially blank. However, if from review of the entire SAR, there was information to indicate that the filing institution was not in a position to obtain the missing information, we did not treat the field as missing or incomplete.

We considered the information in a SAR field as inappropriate if the information was clearly incorrect or inconsistent with instructions or intent. For example, a U.S. state was shown as the issuer of a passport. Finally, we considered a SAR field as inconsistent if information in the field conflicted with information in the narrative section.

At the request of FinCEN, we also reviewed each paper SAR against the SAR System record to determine if the data transcription contractor met contract accuracy requirements. We disregarded trivial discrepancies that neither changed intended meaning, nor resulted in loss of information.

We also used the sampled SARs to measure SAR timeliness from two respects: (1) how long it took between the date of the suspicious activity and the date the SAR was filed by the institution, and (2) how long it took the IRS to process the SAR upon receipt. Together these time periods provided an indicator as to how quickly law enforcement had access to SAR information. The measured timeframes were based on a combination of actual recorded dates from the SAR and estimated timeframes (e.g., posting to the system) provided by IRS officials. Estimated timeframes were predominately used for the posting date for all SARs, and the date IRS received electronic SARs.

To obtain further insights on the causes of SAR data quality problems, we contacted 10 DIs, and 5 MSBs from our sample. We obtained their perspectives on problems encountered when filing SARs, as well as the adequacy and accessibility of FinCEN's SAR guidance.

Appendix 1

Objectives, Scope and Methodology

Review of SAR Processing Controls

Through direct observation, review of applicable documents, and interviews, we documented SAR processing steps. We focused on controls to ensure that SARs are complete and accurate, and that all SARs are entered onto the data base.

Duplicate SARs

We initially inquired with FinCEN officials as to the status of any corrective action taken to address the 3,000 duplicate SARs noted in our December 2002 report. Upon determining the duplicate SARs had not been purged or flagged for end-users, we updated, through FinCEN, the extent of duplicate SARs, and also discussed the methodology used to identify duplicate filings.

Audit Coordination

In planning our detailed review at the IRS DCC, we coordinated with the Treasury Inspector General for Tax Administration (TIGTA) to ensure that we would not duplicate TIGTA ongoing or recently completed audits. We also inquired as to any TIGTA audit findings related to SAR data quality.

We conducted our audit from June 2003 through November 2004 in accordance with generally accepted government auditing standards.

Appendix 2

Number of Sampled SARs With Data Quality Problems Affecting Investigative Fields

SARs With Problems in:	DIs	MSBs	Total
1 – 4 Fields	99 (49%)	92 (45%)	191
5 – 8 Fields	13 (6%)	34 (17%)	47
9 - 23 Fields	0 (0%)	9 (4%)	9
SARs With Problems	112 (55%)	135 (67%)	247
SARs Without Problems	91 (45%)	68 (33%)	159
Total SARs Sampled	203 (100%)	203 (100%)	406

Source: OIG Analysis

Appendix 3

Projected SARs With Data Quality Problems

DIs versus MSBs

Type of Filer	SARs in Population	Estimated Number of SARs With Problems		Sampling Error ± %
		Minimum	Maximum	
DIs	285,336	139,610	178,055	6.7 %
MSBs	130,180	80,761	96,232	5.9 %
DI & MSB Combined	415,516	227,669	266,989	4.7 %

Source: OIG Analysis

With sample stratification, the overall sample precision (sampling error) becomes smaller than that of each stratum.

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FinCEN's Revised Corrective Action Plan



DEPARTMENT OF THE TREASURY FINANCIAL CRIMES ENFORCEMENT NETWORK

September 3, 2004

MEMORANDUM FOR BENNY W. LEE
REGIONAL INSPECTOR GENERAL FOR AUDIT

FROM: *WFB* William F. Baity, Deputy Director

SUBJECT: *Audit follow-up status to Audit Report OIG-03-035 (FinCEN: Reliability of Suspicious Activity Report, December 18, 2002)*

This memorandum provides an update on FinCEN's action plan in response to the Audit Report entitled "Reliability of Suspicious Activity Report," dated December 18, 2002. We have attached a table outlining action items from that audit and the status of each item (see attachment A). We have also attached our comprehensive plan outlining the actions that we have taken and will take to enhance data integrity and to decrease the incidence of duplicate suspicious activity reports. This plan goes beyond the audit completed in December, 2002, as it addresses suspicious activity reports for all affected industries, not just depository institutions (see attachment B).

Among other important steps, based on a successful pilot project, FinCEN will identify financial institutions with apparent systemic suspicious activity report quality problems through the quarterly review of electronic reports identifying blank fields and possible duplicate reports. Once identified, FinCEN will notify the federal agency responsible for examining the financial institution for Bank Secrecy Act compliance, or, where appropriate, FinCEN will contact the financial institution directly. FinCEN will maintain a list of filers with systemic data quality issues to ensure that progressive remedial steps are taken.

As the administrator of the BSA, I acknowledge that the reliability of suspicious activity report data is vital to accomplishing FinCEN's core mission. We will continue to strive for improvement in both the completeness and accuracy of the data within the parameters established by the Bank Secrecy Act and our implementing regulations, as well as in dissemination of this important information to law enforcement nationwide.

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FinCEN's Revised Corrective Action Plan

ATTACHMENT A

Financial Crimes Enforcement Network

Plan to Address Suspicious Activity Report Data Quality

Outlined below are the steps that the Financial Crimes Enforcement Network (FinCEN) will take to enhance the quality of data received by FinCEN in suspicious activity reports filed pursuant to the Bank Secrecy Act and FinCEN's implementing regulations. FinCEN has prepared this plan as part of its ongoing commitment to improving the quality and utility of information reported pursuant to the Bank Secrecy Act, as well as in response to data quality problems identified by the Office of the Inspector General. Accordingly, FinCEN will adjust this plan as may be necessary or appropriate when the Office of the Inspector General completes its follow up audit and presents findings to FinCEN.

Data Quality Issues

In a December 2002 report and throughout the course of consultations with FinCEN during a pending follow-up audit, the Office of the Inspector General has identified the following concerns with suspicious activity report data:

- *The existence of duplicate suspicious activity reports, that is, reports containing identical or nearly identical information but with distinct DCC document control numbers.*

Duplicative reports result from filers erroneously submitting the report to the IRS Detroit Computer Center (IRS-DCC) twice, typically because of problems with the filers' automated filing systems.

- *Suspicious activity reports with blank data fields.*

Data fields on suspicious activity reports may be left blank by filers for a variety of reasons. For example, the form may request information that is not known or available to the filer. Moreover, the usefulness of the form to law enforcement regardless of the missing information will depend on the type of filer, the fields that have been left blank and the reasons therefore. Certain fields, such as the narrative section, are essential to the value of the report.

FinCEN's Plan to Enhance Data Quality

FinCEN believes that steps can and should be taken to enhance the quality of information provided in suspicious activity reports. But FinCEN's response must be measured against the scope of the problems identified and the compelling need to devote resources to other important activities that enhance the effectiveness of the Bank Secrecy Act. Accordingly, FinCEN has taken and will continue to pursue the following steps to address the data quality issues described above:

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1. Duplicate Suspicious Activity Reports

FinCEN has evaluated alternative approaches to deal with the duplicate suspicious activity reports posted to the database, including the costs associated with enhanced internal controls. As part of this review, FinCEN contacted representatives of key law enforcement agencies to seek a consensus on removal and archiving of this data. The response was that removal of duplicate reports would result in confusion and a disruption in the ability to track cases because even a “duplicate” suspicious activity report has a unique Document Control Number (DCN). Database users identify and refer to documents by the DCN. The DCN is a fourteen-digit number assigned by the IRS-DCC when the suspicious activity report is received, and before it is posted to the database. It is a sequential number unique to each document and includes a form code that identifies the document type.

Rather than remove duplicate suspicious activity reports from the database, FinCEN will take the following proactive and corrective actions:

- *Outreach and Education*

FinCEN will expand outreach to industry focused on decreasing the number of paper and magnetic media filings (which are most vulnerable to filing error) and substantially increasing electronic filings via the Patriot Act Communications System. (An increase in electronic filings should correlate to a reduction of duplicate suspicious activity reports.)

- *Identification of and Outreach to Filers with Systemic Duplicate Filing Issues*

While FinCEN has determined that it is impractical and inefficient to pursue individually each filer that submits a duplicate suspicious activity report, FinCEN will take reasonable steps, through an automated review, to identify filers with systemic or pervasive duplicate filings. Once identified, FinCEN will contact the financial institution directly to advise them of the problem and determine whether remedial action is necessary. FinCEN will maintain the list of filers with systemic duplicate filing problems to ensure that progressive remedial steps are taken when necessary.

To identify systemic duplicate filings, every quarter, FinCEN will receive an electronic report that identifies all suspicious activity reports that may be duplicates.¹ FinCEN will review the quarterly report to attempt to identify filers with systemic or pervasive compliance issues and take the steps described above. The concept of systemic or pervasive is necessarily flexible. FinCEN will have a better assessment of the thresholds for taking action once we have experience analyzing the data.

¹ “Duplicate” means that there is a 100% content match between two or more records.

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- *Explore Technology Options to Flag or Indicate Possible Duplicate Records*

As part of the requirements phase of FinCEN's Bank Secrecy Act data repository "BSA Direct" project, FinCEN will evaluate options for alerting users of the data of possible duplicate records. This would allow FinCEN analysts, law enforcement and regulators to adjust or indicate in their analytical efforts where data may contain duplicates.

2. Blank Data Fields

As with the duplicate report issue, FinCEN has evaluated alternative approaches for reducing the occurrence of blank data fields. FinCEN will seek to reduce the occurrence in the following manner:

- *Outreach and Education*

The focal point of FinCEN's efforts to enhance data quality will continue to be outreach to, and education of, filers. This will be accomplished through a variety of techniques including, emphasizing suspicious activity reporting data quality in public speeches, presentations, and training opportunities, as well as issuing periodic written guidance describing reporting deficiencies.

- *Identification of, and Outreach to, Filers with Systemic Data Quality Issues*

While FinCEN has determined that it is impractical and inefficient to pursue each filing of a suspicious activity report with blank or incomplete data fields, FinCEN will take reasonable steps to identify programmatically filers with systemic or pervasive blank "critical" data fields. Once identified, FinCEN will notify the federal agency responsible for examining the financial institution for compliance and request follow up with the financial institution. Furthermore, in egregious cases, FinCEN will contact the financial institution directly to determine whether remedial enforcement action is necessary. FinCEN will maintain the list of filers with systemic data quality issues to ensure that progressive remedial steps are taken when necessary.

As a first step in developing a process to programmatically identify suspicious activity reports with blank fields, FinCEN initially identified the following fields as critical:

- Filer name
- Type of Suspicious Activity
- Narrative
- Primary Regulator
- ZIP of Branch Where Activity Occurred
- Suspect Name
- Suspect SSN

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- Suspect DOB
- Suspect Address

FinCEN identified these fields based on its own knowledge, experience, and expertise as well as through consultations with law enforcement liaison. FinCEN believes that the process of determining which fields are critical is iterative. We are now working to determine whether the list should be expanded, and we look forward to working with the Inspector General to further refine this list going forward.

On a quarterly basis, FinCEN will review electronic reports that identify suspicious activity reports with blank critical data fields. From this, FinCEN will be able to identify filers with systemic or pervasive occurrences of blank fields and take the steps described above to contact the primary federal regulator or reach out to the institution directly. As noted previously, the concepts of systemic and pervasive are necessarily flexible. FinCEN will have a better assessment of the thresholds for taking action once we have experience with the data.

In December of 2003, FinCEN received a report of suspicious activity reports filed with blank critical data fields. On the basis of this information, FinCEN referred 32 financial institutions with systemic filing errors to their primary federal regulator.

By utilizing this approach, FinCEN will have the ability to continue to monitor the occurrence of blank critical data fields and determine whether these efforts are having a positive impact.

- *Explore Enhanced Data Perfection Opportunities in the Electronic Filing Environment to Address Blank Fields*

FinCEN strongly believes that technology can be of enormous value in addressing data quality problems. The BSA Direct project (scheduled for delivery in the Fall of 2005) will include data quality tools to screen, perfect, normalize and flag data as it enters the BSA Direct data warehouse. A similar emphasis on technical data quality disciplines and tools is being pursued in FinCEN's e-Filing (PACS) project, to apply cost-effective data perfection mechanisms to eliminate duplicate filings and notify filers of incomplete or blank data fields before the reports are submitted.

- *Revise Suspicious Activity Forms to Emphasize Completeness and Offer Assistance to Filers*

FinCEN will revise its suspicious activity reporting forms to better emphasize the need to provide complete information. Additionally, the forms will remind filers to contact FinCEN or the institution's primary federal regulator for assistance. Each form will be revised as part of the routine revision schedule. For depository institutions, the SAR Owners Group has recommended that this be done in conjunction with the form renewal in FY 2006.

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FinCEN's Revised Corrective Action Plan

ATTACHMENT B

FinCEN SAR-DEPOSITORY INSTITUTIONS DATA QUALITY IMPROVEMENT ACTION PLAN

This action plan covered only Depository Institutions since all other industries had only been reporting a few years.

Issue	Milestone/Action	Planned Date	Status
Blank Fields			
	Evaluate incidence of blank field for 2001 & 2002	FY 2004 1 st Qtr	Completed.
	Evaluate incidence of blank field for 2003	FY 2004 3 rd Qtr	Completed
	Evaluate for filers with systemic or pervasive incidences of blank fields. Refer such institutions to their primary federal regulator for action.	FY 2004 2 nd	Completed review. Sent five letters to various federal regulators referring a total of 32 financial institutions with systemic blank field issues.
	Develop analysis reports to periodically review filings and identify financial institutions with systemic or pervasive occurrences of blank fields.	FY 2005 1 st Qtr	
	Evaluate incidence of blank fields periodically to identify systemic or pervasive occurrences with referrals to the federal regulator and/or direct contact with financial institutions as appropriate.	Periodic Review	Ongoing
Outreach			
	Implement an outreach strategy to improve data quality. Include SAR quality as topic in BSA presentations	FY 2003 2 nd Qtr	Completed.
	Enhance focus on SAR data quality through targeted briefing and outreach.	FY 2004 2 nd Qtr	Completed.
	Establish Outreach Schedule for next year and track results.	FY 2005 1 st Qtr	
Duplicate Reports			
	Preliminary assessment of the # of duplicate SARS in the depository institution database with IRS-DCC	FY 2004 3 rd Qtr	Completed
	Discuss potential impact of archive duplicates with regulatory and law enforcement customers	FY 2004 3 rd Qtr	Completed
	Develop analysis reports to monitor and identify financial institutions with duplicate filing and implement a process to review the duplicates periodically.	FY 2004 4 th Qtr	Completed.
	Evaluate incidence of duplicate reports periodically and evaluate for systemic or pervasive duplicate filing, reaching out to such institutions to correct the problem.	Periodic Review	Ongoing
	Evaluate technology options related to duplicate report issue in design phase of BSA data repository.	FY 2005 1st Qtr	


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DEPARTMENT OF THE TREASURY
FINANCIAL CRIMES ENFORCEMENT NETWORK

March 15, 2005

MEMORANDUM FOR DIRECTOR LEE
(WESTERN FIELD AUDIT OFFICE)

FROM: William J. Fox, Director 
SUBJECT: *Management Response to Follow-Up Audit of Financial
Crimes Enforcement Network's Suspicious Activity Reports
Data Quality*

The Financial Crimes Enforcement Network is committed to the effective implementation of the Bank Secrecy Act as it is critical to protecting our financial system and our national security. A central purpose of the Bank Secrecy Act is to ensure the collection of data useful to law enforcement and others engaged in the fight against terrorism and financial crime. As a result, we welcome the work of the Office of the Inspector General in reviewing the quality of data provided by financial institutions in their suspicious activity reports.

The recommendations contained in this Report, when considered contextually and accorded the appropriate level of priority in view of the many important compliance issues, will assist us in better ensuring that suspicious activity reports contain as much useful information as is available to filers. This will maximize their utility to law enforcement and other consumers of the data. We will implement the recommendations, in the manner outlined below.

However, we think it essential that the Report be placed in the appropriate context. First, while we do not dispute that reasonable efforts should be made to ensure that quality information is provided in suspicious activity reports, undue focus on data quality may well skew the perspective of the filers and actually undermine the overall effectiveness of suspicious activity reporting programs within financial institutions by creating distorted incentives. The suspicious activity report is designed to provide leads, not established evidence. Second, the Report can be read to portray unfairly the level of industry compliance with the suspicious activity reporting rules. While the Report acknowledges certain assumptions and inherent research limitations, such caveats to the Report's conclusions are not readily apparent.

Our approach to enhancing data quality is targeted toward education and outreach to the financial industry, combined with a periodic analysis of reports filed and the pursuit of appropriate remedial action against filers with systemic data quality issues. We take this approach in lieu of inflexible rules preventing suspicious activity reports with blank or incomplete fields from being filed in the first instance. While we are seeking to enhance data perfection capabilities on the front end, which will assist filers in ensuring

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that fields are completed, we cannot risk a delay in an even imperfect report being placed in the database when it may be critical to law enforcement.

We readily acknowledge that FinCEN's response to the initial 2002 Report was unacceptable. Management concurred with the recommendations, yet failed to implement them. In 2004, however, following the appointment of Director Fox, we provided the Office of Inspector General with a revised corrective action plan that, as the Report does note, addresses most of the original weaknesses identified. We have also worked closely with the Office of Inspector General to better ensure that the recommendations contained in this report will improve data quality.

Also in 2004, FinCEN expanded dramatically its role in the administration of the Bank Secrecy Act, including creating an entirely new office to support the examination function performed by other agencies and devoting one-third of its analytical resources to regulatory compliance support. This expansion – with an accompanying augmentation in resources – will better enable us to identify and address data quality problems associated with suspicious activity reports. Both our renewed commitment to work together with the Office of the Inspector General on these issues as well as our realignment and mission expansion should be reflected prominently in this Report.

Our response to the specific recommendations are set forth below. At the outset, we have the following observations:

- *The suspicious activity report is a lead for investigators.*

The suspicious activity report was designed to provide law enforcement with lead information, akin to a confidential informant's tip. It contains the suspicions of the filer rather than proven facts. This important perspective is lost in the Report. We fear that the Report suggests a zero tolerance for errors or omissions in a broad array of data fields deemed "critical," but not identified. Yet we all agree that this is not the goal.

- *Suspicious activity report data quality is but one of many important Bank Secrecy Act compliance issues.*

As the delegated administrator of the Bank Secrecy Act, we have the obligation to determine where we will devote our resources to ensure the effective implementation of the Act. Without discounting the importance of data quality, a potential danger with a report of this nature is that by focusing on a single aspect of compliance, it may well lead filers to do the same. This concern is amplified by the Report's assertion that over half of the suspicious activity reports are problematic because one or more critical fields are blank or contain inappropriate information, even though all agree that it is impossible to assess whether those suspicious activity reports are of less value to law enforcement on an aggregate basis. We should and will take reasonable steps to implement the

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recommendations as explained below. It is also important, however, to maintain an informed perspective on these tasks in light of the many critical functions that this agency performs.

- *Key findings have important limitations that, while acknowledged in the Report, should be emphasized.*
 - *The conclusion that 62% of the suspicious activity reports filed contained data quality problems is potentially misleading.* “Problem” suspicious activity reports include those reports filed with a single field missing, such as the phone number of the suspect – such information may be difficult or impossible to obtain, and certainly cannot alone serve as the foundation for concluding that the report is of little value. In fact, whether a missing field affects the value of a suspicious activity report will depend on the facts and circumstances of each individual report – the impact of fields with missing or inadequate information cannot be quantified statistically. It is often the case that filers will not have all the information sought on the form, typically because the reports are the product of sophisticated “back-end” analyses of information. We should continue to encourage such analysis and filing.
 - *There may be legitimate, indeed compelling, reasons why information may not be provided in a suspicious activity report.* If a filer does not have certain information – because the information is not available or is perhaps unknowable – the corresponding suspicious activity report would not be erroneous by virtue of not containing such information. There are categories of filings where information will always be missing because of the nature of the transaction, such as reports on nested correspondent accounts and other clearing services, where we nonetheless want to encourage continued filing. In addition, even with blank fields or fields containing inconsistent information, the narrative section provides critical analysis, and may ultimately provide more information to law enforcement than any other field. Without discounting the importance of other fields, we will continue to focus on ensuring that filers provide a comprehensive description in the narrative section.
 - *The Report does not provide the information necessary to determine whether a suspicious activity report was timely filed.* The sole basis articulated for this finding is the timeframe between the conclusion of the suspicious activity, as provided in the suspicious activity report, and the date the report was filed. But this information alone does not conclusively establish whether the suspicious activity report was filed within the prescribed regulatory timeframe because the date the activity was discovered is not reported. Moreover, we believe it essential that financial institutions utilize the allotted time for filing

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a suspicious activity report to ensure that the facts are reviewed and the reports receive appropriate senior level review before they are filed.

- *The criticism leveled against reports filed by Money Services Businesses must be measured against the realities of compliance in the industry.* The Money Services Business industry ranges from several large, highly sophisticated services providers to a countless number of small “mom and pop” businesses that speak no English. Compliance in this industry remains a central focus of FinCEN, but the reality is that the task of ensuring the implementation of the most basic of recordkeeping and reporting requirements in large segments of this highly diverse and fluid industry continues to be a significant challenge for all parties involved. While we have taken, and will continue to take, appropriate enforcement actions against Money Services Businesses when warranted, we will continue to focus our resources on identifying these businesses and educating them on the requirements of our regulatory regime.

FinCEN Responses to Recommendations:

Recommendation 1: Based on results of our sample, establish a position for a BSA data administrator (i.e., data integrity officer) with specific responsibility for ensuring the accuracy and timeliness of the SAR data system, or assign this responsibility to an existing position. We believe this position would be better situated by reporting directly to FinCEN, rather than the IRS.

Response: Concur with comment. As the administrator of the Bank Secrecy Act, we agree with the concept of ensuring that appropriate attention is given to Bank Secrecy Act data integrity and for improving the data quality through reasonable means. We further concur that this should be done by holding appropriate officials accountable. However, given FinCEN’s organizational structure and management theory, we believe that this is best achieved by assigning this responsibility to existing positions within FinCEN, while ensuring appropriate coordination and accountability.

The responsibility for ensuring suspicious activity report data quality falls within three FinCEN divisions – the Analytics Division, Regulatory Policy and Programs Division, and Client Liaison Services Division. Within those divisions, we will assign responsibility to the following individuals who will be jointly responsible for data integrity and carrying out the recommendations contained in this Report: The Assistant Director, Office of Regulatory Support, Analytics Division; the Assistant Director, Office of Compliance, Regulatory Policy and Programs Division; and the Assistant Director, Office of BSA Data Services, Client Liaison Services Division. Status: Target completion – April 31, 2005.

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Recommendation 2: Establish measurable standards to address at least two data quality aspects: critical data fields that are responsive to law enforcement needs, and an acceptable level of data quality.

Response: Concur with comment. We concur with the recommendation that FinCEN should establish measurable standards to address critical data fields and an acceptable level of data quality. For example, 'critical' fields (which require completion if the information is known to the filer) were established for the casino suspicious activity report from dated April 2003 and for the futures report form dated May 2004. Moreover, plans were made to add critical fields to all forms as they required renewal/revision.

Critical Data Fields – The identification of critical data fields must be made in consultation with not only law enforcement, but also with financial institutions that file reports and other consumers of the data, namely, federal regulators of the financial institutions. Moreover, the identification must be made in a manner consistent with our policy goals and objectives for the suspicious activity reporting regime, understanding that blank fields may be unavoidable or justifiable. It is essential to develop the list of critical data fields with due regard to all interests affected. **Status:** Target completion – September 30, 2005.

Acceptable Level of Data Quality – Once critical fields have been identified, we will establish the criteria for our quarterly analysis. Prior to identifying the criteria, we will need to obtain baseline data based on the revised critical fields. Once established, we will be in a position to determine whether our identification, outreach, and remedial actions described in our September 3, 2004 Revised Corrective Action Plan, as modified herein, is meeting our expectations. **Status:** Target completion – December 1, 2005.

Recommendation 3: Establish a process to periodically include input from law enforcement case agents for a contemporary investigative perspective.

Response: Concur with comment. As noted above, we will solicit input not only from law enforcement, but also from financial institutions that file suspicious activity reports as well as the regulators. We note that in addition to consultations with our law enforcement liaisons to FinCEN, we currently seek input from these sources at least every three years during the form renewal process, and more frequently when forms are amended. However, we will establish a procedure for the periodic solicitation of additional input. **Status:** Target completion – September 30, 2005.

Recommendation 4: Assess the need to identify the specific data fields associated with the 15,000 duplicates and advise law enforcement so that they may better gauge the potential impact of duplicates. Duplicate SARs involving certain crimes may be of more importance to certain law enforcement agencies given their differing authorities over certain crimes such as credit card fraud versus mortgage loan fraud.

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Response: Concur. We will analyze a sample of duplicate records to assess whether the duplicates may affect statistical summaries of the suspicious activity report data.

Status: Target completion- September 30, 2005.

Recommendation 5: Assess the need and feasibility of identifying, tagging or segregating duplicate SAR filings into a suspense file until a more systematic process can be devoted to prevent them from being entered into the system.

Response: Concur. As set forth in our Revised Corrective Action Plan of September 3, 2004, we have already considered and, following consultation with law enforcement, rejected the idea of removing from the database and archiving duplicate suspicious activity reports. As noted, law enforcement requested that duplicate reports not be removed from the database as this would result in confusion and a disruption in their ability to track cases.

Instead, given that duplicate reports comprise a very small fraction of the overall reports in the database, our corrective action will focus on education and outreach, identifying, on a quarterly basis, filers with systemic and pervasive duplicate filings and taking appropriate action to reach out to such filers to correct the problem. We will also explore new technology to flag for users duplicate reports in our Bank Secrecy Act data repository project that is currently under development – “BSA Direct.” This would allow FinCEN analysts, law enforcement and regulators to adjust or indicate in their strategic analysis efforts where data may contain duplicates. Finally, we will explore the possibility of using this new system to identify and prevent duplicate reports from being filed. Within the current database, it is not feasible to identify or segregate duplicate suspicious activity reports. We will, however, attempt to use the new technology of the BSA Direct system to flag duplicates. **Status:** Complete.

Recommendation 6: Advise and solicit the views of law enforcement agencies as to whether the observed timeframes are responsive to their needs. In so doing, FinCEN will be better positioned to assess any needed changes, such whether filer outreach or supervisory oversight should be focusing on the timely filing of SARs.

Response: Concur. When we solicit the views of law enforcement, we will also solicit the views of the federal regulators that supervise these institutions. Additionally, we will note that the timeframes observed in the report alone do not indicate that our regulations were violated. **Status:** Target completion – December 1, 2005.

Recommendation 7: Assess the need to review timeliness as part of the planned quarterly SAR reviews for indications of potential violations of regulatory filing timeframes.

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Response: Concur. FinCEN will assess the feasibility of extracting accurate data on filing timeframes from the suspicious activity report database. As noted above in our management response, conclusive data may be difficult to obtain. However, we will assess the feasibility of identifying financial institutions that may be pervasively filing suspicious activity reports after required filing deadlines. If accurate data can be extracted, we will develop procedures for incorporating this data in quarterly reviews. **Status:** Target completion – September 30, 2005.

Recommendation 8: Assess the need to refer any of the identified lengthy filing timeframes (those exceeding 30 or 60 days) to the applicable regulatory agencies to determine whether timely SAR filing is an area warranting detailed examination or enforcement action.

Response: Concur. If feasible pursuant to Recommendation 7, this data will be evaluated to identify and refer financial institutions with pervasive filing deficiencies to the applicable regulatory agency for possible follow-up action. Under such circumstances we may also choose to initiate follow-up action. **Status:** Target completion – December 1, 2005.

Recommendation 9: Assess the adequacy and consistency of regulators' examination handbooks covering financial institutions' compliance with the BSA SAR filing requirements. This assessment should include the need to clearly spell out examiners responsibilities; and the examination procedures to determine whether institutions are filing accurate, complete, and timely SARs.

Response: Concur. We have implemented this recommendation. We are currently working with the five Federal banking agencies in drafting interagency Bank Secrecy Act/Anti-Money Laundering examination procedures. At our request, guidance on suspicious activity report quality was added to the draft examination manual. To evaluate suspicious activity report quality, an examination procedure was added in the Suspicious Activity Reporting section of the manual, which directs examiners to sample reports filed by the subject institution. In addition, FinCEN drafted an appendix to the examination manual detailing standards of effective suspicious activity report narratives and referencing FinCEN's publication, Guidance on Preparing a Complete and Sufficient Suspicious Activity Reporting Narrative, from November 2003.

Separately, we have reviewed and provided written suggestions to the examination manual of the Internal Revenue Service, the regulator responsible for examining Money Services Businesses. We recommended adding a direction to examiners to conduct specific review of an institution's policies, procedures and internal controls to identify potential weaknesses and deficiencies that could result in failures to properly file suspicious activity reports, as well as to sample reports filed by the institution to

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determine the level of accuracy and completeness of the reports and failures to file reports. **Status:** Completed

Recommendation 10: Establishes policies and procedures for timely routine follow-up on regulatory referrals to federal regulators to determine their supervisory resolution.

Response: Concur. Appropriate procedures will be established for routine follow-up on referrals to federal regulators as part of the development of the Office of Compliance. Once the Office of Compliance has an acceptable level of staffing in place and systems, policies, and procedures are developed, follow-up on referrals to other agencies will be routine. **Status:** Target completion – December 1, 2005.

Recommendation 11: Assess the need for either enhanced outreach or supervisory enforcement action with the three MSBs accounting for over 77% of the problem MSB SARs in our sample.

Response: Concur. We have assessed the issue, engaged in enhanced outreach, and, where appropriate, taken other regulatory action against these entities. These enhanced compliance activities have been completed in conjunction with pending or completed enforcement actions. **Status:** Completed.

Recommendation 12: Assess the need to expand the number of data fields subject to keystroke verification to include data fields critical to law enforcement.

Response: Concur. We will review the contract between the Detroit Computing Center and the standards outlined for keystroke verification. (Keystroke verification will only result in correction of typos not in the addition of information that is available to the keyer.) We will request reports presently used by the IRS to ensure contractor adherence to requirements. **Status:** Target completion – December 30, 2005

Recommendation 13: Reassess how the contractor's 3% performance standard is to be measured so as to give greater consideration to the number of SARs with errors rather than just the total number of errors. This would provide added perspective to situations where a few SARs account for a large number of errors as opposed to a large number of SARs each with a few errors.

Response: Concur. FinCEN will establish a process to periodically obtain input from DCC as to how the 3% error rate is monitored and the actual number of suspicious activity reports involved. We would like to highlight the processing time for suspicious activity reports. As detailed in the Report, from IRS-DCC receipt to posting in the database, suspicious activity reports were processed and posted to the system within 3 days on average for electronically filed reports, and within 10 days on average for paper

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reports; a very reasonable timeframe given the volume of reports processed by IRS-DCC.
Status: Target completion – October 31, 2005

Recommendation 14: Assess whether the scope of the contract could be economically and feasibly expanded to identify SARs with missing and or incomplete data fields. This might provide FinCEN with a means of identifying egregious problem filers in a timelier manner than the quarterly reviews noted in the revised corrective action plan. This would also cover the majority of SARs since most SARs are filed by paper.

Response: Concur in concept. FinCEN has assessed a number of options for identifying SARs with missing or incomplete data fields, including the recommendation above. The current data entry process uses business practices that are mechanical and repetitious with emphasis on a combination of speed and accuracy performance standards. The addition of analysis of missing or incomplete fields would be incompatible with their current performance standards and business practices.

FinCEN also examined a number of options including a correspondence program to obtain additional information from the filers, using technology to flag SARS with missing or incomplete data fields, creating a quarterly report to identify records needing follow-up for certain types of data quality issues, and effects of electronic filing. FinCEN has determined that using information technology to identify records needing further analysis is the most cost effective approach. Based on this analysis, FinCEN began a process to receive computer-generated reports quarterly with highlights to certain types of data quality issues.

The longer-term technology solutions include FinCEN's BSA Direct project and accelerating electronic filing. A key design feature of FinCEN's BSA Direct project is the use of sophisticated data cleansing techniques that will automatically elucidate certain problems and dramatically improve the overall quality of the BSA data. BSA Direct will be operational in October 2005 so it is impractical to implement other temporary measures at this time. Also, we are observing significant trends related to a growing number of paper filers using BSA E-Filing system to file their SARs. Each quarter we notice a decrease in the percentage of paper filing, even while the percentage of BSA E-filing is continuing to grow. For example, total SARs filed through BSA e-filing as of September 2004 were as follows: E-filing 17%, paper 57%, and magnetic media was at 26%. By the end of December 2004, total SARs filed using electronic filing increased significantly in just three months as follows: E-filing 34%, paper 46%, and magnetic media 20%. FinCEN's efforts will continue to focus on the longer-term technology based solutions to improve SAR data quality. Status: Completed.

Appendix 6

Major Contributors to This Report

Western Field Audit Office

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Appendix 7

Report Distribution

Department of the Treasury

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